

Box 7

RESULTS OF THE ECB SURVEY OF PROFESSIONAL FORECASTERS FOR THE THIRD QUARTER OF 2010

This box reports the results of the ECB Survey of Professional Forecasters (SPF) for the third quarter of 2010. The survey was conducted between 14 and 19 July 2010. There were 55 responses from forecasters. The SPF collects information on expectations for euro area inflation, real GDP growth and unemployment from experts affiliated with financial or non-financial institutions that are based in the EU.¹

Inflation expectations for 2010, 2011 and 2012

Compared with the previous SPF round, forecasters have not changed their outlook for inflation: expectations remained unchanged at 1.4% for 2010, 1.5% for 2011 and 1.7% for 2012 (see the table).²

The SPF inflation expectations for 2010 and 2011 are within the ranges reported in the June 2010 Eurosystem staff macroeconomic projections. Compared with the forecasts of the July 2010

1 Given the diversity of the panel of participants, aggregate SPF results can reflect a relatively heterogeneous set of subjective views and assumptions.

2 Additional data are available on the ECB's website at www.ecb.europa.eu/stats/prices/indic/forecast/html/index.en.html

Results of the SPF, Eurosystem staff macroeconomic projections, Consensus Economics and Euro Zone Barometer

(annual percentage changes, unless otherwise indicated)

HICP inflation	Survey horizon					
	2010	June 2011	2011	June 2012	2012	Longer-term ²⁾
SPF Q3 2010	1.4	1.4	1.5	1.7	1.7	2.0
Previous SPF (Q2 2010)	1.4	-	1.5	-	1.7	1.9
Eurosystem staff macroeconomic projections	1.4-1.6	-	1.0-2.2	-	-	-
Consensus Economics (July 2010)	1.5	-	1.5	-	1.5	2.0
Euro Zone Barometer (July 2010)	1.4	-	1.5	-	1.6	1.9
Real GDP growth	2010	Q1 2011	2011	Q1 2012	2012	Longer-term ²⁾
SPF Q3 2010	1.1	1.4	1.4	1.4	1.6	1.8
Previous SPF (Q2 2010)	1.1	-	1.5	-	-	1.8
Eurosystem staff macroeconomic projections	0.7-1.3	-	0.2-2.2	-	-	-
Consensus Economics (July 2010)	1.1	-	1.4	-	1.6	1.8
Euro Zone Barometer (July 2010)	1.1	-	1.3	-	1.6	2.0
Unemployment rate ¹⁾	2010	May 2011	2011	May 2012	2012	Longer-term ²⁾
SPF Q3 2010	10.1	10.2	10.2	9.9	9.8	8.4
Previous SPF (Q3 2010)	10.3	-	10.3	-	-	8.5
Consensus Economics (July 2010)	10.1	-	10.2	-	-	-
Euro Zone Barometer (July 2010)	10.2	-	10.2	-	10.0	8.8

1) As a percentage of the labour force.

2) Longer-term inflation expectations refer to 2014 in the Euro Zone Barometer and to 2015 in the SPF for the third quarter of 2010 and Consensus Economics. Expectations for 2012 and the longer-term expectations for Consensus Economics are from the April 2010 release.

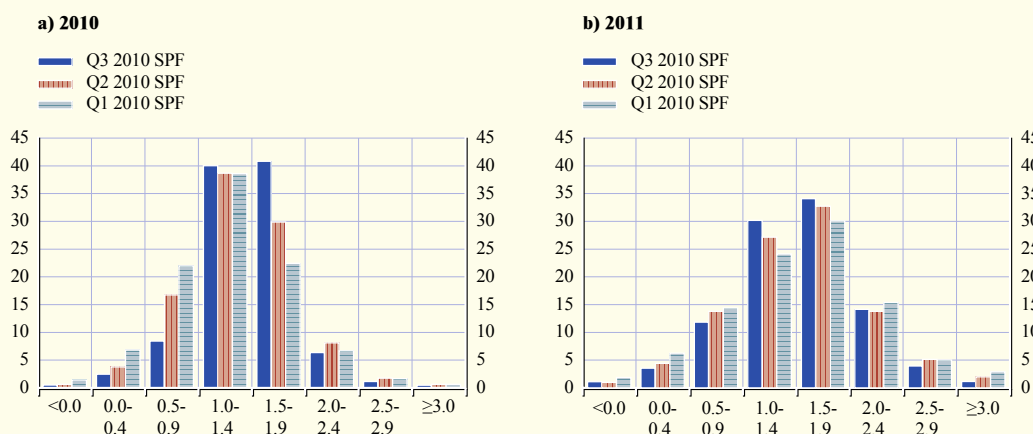
issues of Consensus Economics and the Euro Zone Barometer, the SPF inflation expectations are broadly similar for 2010 and 2011, and slightly higher for 2012.³

The SPF participants were also asked to assess the probability of inflation falling within specific intervals. Compared with the previous SPF round, the aggregate probability distribution for 2010 is now more concentrated in the range between 1.0% and 1.9%, as respondents now assign

³ Consensus Economics forecasts for 2012 were published in the April 2010 release.

Chart A Probability distribution for average annual inflation in 2010 and 2011 in the latest SPF rounds¹⁾

(probability in percentages)



Source: ECB.

1) Corresponds to the average of individual probability distributions provided by SPF forecasters.

an 81% probability to this interval. Within this range, the two intervals from 1.0% to 1.4% and from 1.5% to 1.9% have been assigned around the same probability. Respondents have assigned a probability of 11% to a lower inflation outcome (below 1.0%) and a probability of 8% to a higher inflation outcome (above 1.9%). The probability distribution for 2011 has remained broadly stable compared with the previous SPF round, with a slight increase in the probability of inflation outcomes being in the range from 1.0% to 1.9% (see Chart A). Based on the individual probability distributions, the balance of risks to these forecasts is assessed by respondents as being on the downside across all forecast horizons, and in particular for 2012. This is reflected in the fact that the majority of respondents provided a point forecast that is above the mean forecast from their probability distribution, implying that they assign a higher probability to outcomes below this point forecast than to those above it. Most respondents mention low wage growth owing to the high unemployment rate as the main downside risk to the inflation outlook. Many respondents commented that the main upside risks to the baseline scenario are: i) higher import prices owing to the depreciation of the euro; ii) rising raw materials and oil prices; and iii) increases in indirect taxes and administered prices as a result of fiscal consolidation plans.

Indicators of longer-term inflation expectations

Longer-term inflation expectations (for 2015) have been slightly revised upwards, on average, to 2.0% from 1.9% (for 2014) in the previous SPF round. The median of the point estimates, which is less affected by extreme values than the average point estimate, remained at 1.9%. The average point forecast is in line with the long-term inflation projections provided by Consensus Economics in April (at 2.0%) for 2015 and above those of the Euro Zone Barometer (at 1.9%) for 2014, which were published in July 2010.

The slight upward movement in longer-term inflation expectations is combined with a greater disagreement among forecasters in their longer-term inflation expectations, as measured by the standard deviation of their point forecasts. Nevertheless, the majority of respondents provided a point forecast for longer-term inflation expectations in the range from 1.8% to 2.0% (see Chart B).

At the same time, aggregate uncertainty surrounding these inflation expectations, as measured by the standard deviation of the aggregate probability distribution, remained at a level similar to that in the previous SPF round.⁴ Finally, the probability of longer-term inflation standing at 2% or above remained broadly stable at 44%, after 43% in the previous SPF round.

Measures of inflation expectations derived from financial markets have remained broadly unchanged. However, they have generally been higher than SPF forecasts because they incorporate not only the level of expected inflation, but also an additional premium, to compensate bond investors for inflation risks. They have also been more volatile than survey-based measures, not only owing to the volatility of said inflation risk premium, but also to the fluctuation in bond market liquidity conditions since the middle of 2008 (see Chart C).⁵ The volatility observed in these measures should thus be treated with some caution and should not be mechanically interpreted as reflecting revisions in market participants' long-term inflation expectations.⁶

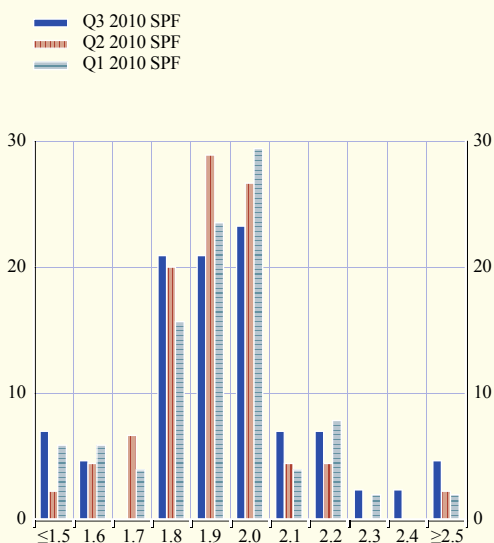
4 For a discussion regarding uncertainty measures, see the box entitled "Measuring perceptions of macroeconomic uncertainty", *Monthly Bulletin*, ECB, January 2010.

5 See also the article entitled "Measures of inflation expectations in the euro area", *Monthly Bulletin*, ECB, July 2006.

6 For further discussion on the impact of the financial market crisis on market-based measures of inflation expectations, see the box entitled "Recent increases in real yields and their implications for the analysis of inflation expectations", *Monthly Bulletin*, ECB, November 2008. Recent developments in financial market indicators of inflation expectations are discussed in Section 2.4 of the *Monthly Bulletin*.

Chart B Cross-sectional distribution of longer-term (2015) inflation expectations among SPF respondents

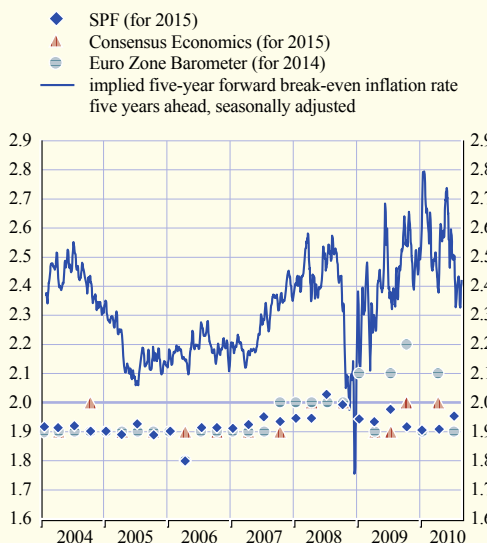
(percentage of respondents)



Source: ECB.

Chart C Longer-term inflation expectations from surveys and break-even inflation rates

(average annual percentage changes; five-day moving averages of daily data)



Sources: Consensus Economics, Euro Zone Barometer, Reuters and ECB calculations.

Real GDP growth expectations

On average, the SPF respondents' expectations for real GDP growth are unchanged at 1.1% for 2010, but have been revised slightly downwards to 1.4% for 2011, from 1.5% in the previous round. In 2012 respondents expect euro area real GDP to grow by 1.6%.

The SPF growth expectations for 2010 and 2011 are within the ranges reported in the June 2010 Eurosystem staff macroeconomic projections for the euro area and broadly in line with the latest Consensus Economics and Euro Zone Barometer forecasts for 2010 and 2011.

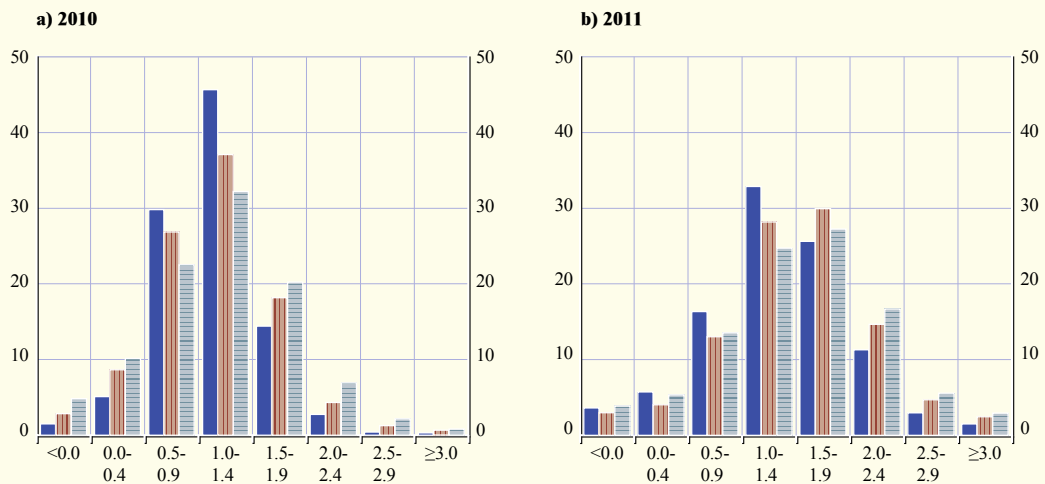
The aggregate probability distribution for 2010 is now more concentrated in the range between 1.0% and 1.4% than in the previous SPF round, as respondents now assign a 46% probability to this interval. With regard to 2011, forecasters now assign the highest probability (33%) to the interval between 1.0% and 1.4% (see Chart D).

The level of uncertainty surrounding one-year-ahead and two-year-ahead real GDP forecasts has not changed from the previous SPF round. The balance of risks to the average point forecast of real GDP growth is assessed to be on downside across all forecast horizons, and in particular for 2012. Several respondents commented that the adoption of fiscal consolidation plans, weaker private consumption and public investment, and heightened financial tensions, in particular tight credit standards, are expected to be downside risks to growth. They also perceived the positive effects of the depreciation of the euro to be the main upside risk to the growth scenario.

Chart D Probability distribution for average annual real GDP growth in 2010 and 2011 in the latest SPF rounds¹⁾

(probability in percentages)

■ Q3 2010 SPF
 ■ Q2 2010 SPF
 ■ Q1 2010 SPF



Source: ECB.

1) Corresponds to the average of individual probability distributions provided by SPF forecasters.

Longer-term growth expectations (for 2015) stand at 1.8%, unchanged from the previous SPF round. The SPF assessment is in line with that of the April issue of Consensus Economics (1.8% for 2015) and below that of the July issue of the Euro Zone Barometer (2.0% for 2014). Looking at the individual probability distributions, respondents assess the balance of risks to longer-term growth to be clearly on the downside.

Expectations for the euro area unemployment rate

Unemployment rate expectations have been revised downwards by 0.2 percentage point for 2010 and by 0.1 percentage point for 2011, to 10.1% and 10.2% respectively. For 2012, they now stand at 9.8%. The balance of risks to short and medium-term expectations is assessed to be on the upside. Longer-term unemployment rate expectations (for 2015) have been revised slightly downwards, by 0.1 percentage point, to 8.4%, and the balance of risks to the longer-term outlook is again assessed to be on the upside.

Other variables and conditioning assumptions

According to other information provided by the respondents, they generally expect: i) oil prices to increase from USD 77 in the third quarter of 2010 to around USD 87 in 2012; ii) wage growth to be at 1.4% in 2010, rising to 1.5% in 2011, 1.9% in 2012 and 2.4% by 2014; iii) the euro to weaken against the US dollar, to stand on average at USD 1.23 in 2011 and USD 1.26 in 2012; iv) the ECB policy rate to remain stable at around 1.0% until the first quarter of 2011 and then increase to around 2.1%, on average, during 2012.